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IN THE

# Supreme Court of the United States

DONALD M. HEAVRIN, PETITIONER

*v.*

J. BAXTER SCHILLING, Trustee

*PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT*

## PETITION FOR WRIT OF CERTIORARI

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## QUESTIONS PRESENTED

1) Where the Bankruptcy Court, acting as the trial court, fails to make a finding of fact on a critical issue, should the Appellate Courts remand the case to the Bankruptcy Court to make that finding of fact?

2) Is a fully assigned life insurance policy part of a bankrupt corporation's estate?

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## OPINIONS BELOW

The decision of the United States Court of Appeals for the Sixth Circuit, 422 F.3d 405, is reprinted as Petitioner's Appendix A.

The Opinion and Order of the United States District Court for the Western District of Kentucky, is reprinted as Petitioner's Appendix B.

The Opinion and Judgment of the United States Bankruptcy Court for the Western District of Kentucky in Case No. 94-32848(3)7, A.P. No. 96-3129 is reprinted as Petitioner's Appendix C.

## JURISDICTION

The Court of Appeals' Judgment was entered August 30, 2005. Rehearing and Rehearing En Banc was denied February 1, 2006. Petitioner's request for an extension of time in which to file this Petition for Writ of Certiorari was granted on April 24, 2006 extending the time in which to file the instant petition to and including July 1, 2006. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. 1254(1).

## RELEVANT PROVISIONS INVOLVED

KRS 304.14-250 (Appendix G)

## STATEMENT

The Bankrupt, Triple S Restaurants, Inc. (TSR) operated Sizzler Restaurants in Kentucky, Indiana, and Ohio. TSR had two major shareholders, Michael R.

Macatee (Macatee) and Robert Harrod (Harrod), who each owned 40% of the stock. They both had other business interests, and each of them set up a trust fund, and their shares of stock in TSR and their other business ventures were transferred to their respective trust funds. The purchase of the Sizzlers was financed by McDonnell Douglas Finance Corporation (MDFC) in 1988. To secure the debt of $3,560,000.00, MDFC required life insurance policies to be purchased on the two largest shareholders. Macatee had four $500,000 life insurance policies (with cash value) for a total of $2,000,000. The Harrod policy was a ten-year annual, renewable-term policy (no cash value), and when the premiums became prohibitive, he purchased a replacement policy (with MDFC's permission) in the amount of $2,000,000. The replacement policy was also a ten-year, annual renewable-term and was purchased in 1991, three years before Harrod died. MDFC made the premium payments on both the Harrod policy and the Macatee policies. Both Macatee and Harrod were Co-makers of the loan and they were both 100% liable for the entire debt. At first, the policies were owned by TSR, but were fully assigned to MDFC to secure the debt[1].

The policy on the life of Harrod was transferred to the Harrod Trust subject to the assignment to MDFC. The beneficiaries of the Harrod Trust were Harrod's children, Donald M. Heavrin (Heavrin) and Bobbie Bridges (Bridges). The ownership of the Macatee policies were transferred to the Macatee Trust subject to

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[1] Several months after Harrod died, Macatee filed Bankruptcy and MDFC, exercising all rights of ownership pursuant to its assignment, cashed the policies and took the cash value.

the assignment to M FC. His daughter was the beneficiary of the Trus

Four months after the transfer of the ownership of the policies, Harrod died. At the time of his death, the debt owed to MDFC was about $3.4 million. Despite this fact, Heavrin, acting on behalf of the Harrod Trust, asserted a lender-liability claim against MDFC. MDFC refused to settle any claim that had a lender-liability label attached to it because it did not want to establish a precedent. However, MDFC agreed to share the proceeds of the life insurance policy for a complete release from the Harrod Trust. One year before Harrod died, there had been a number of discussions about lender liability and damages that MDFC had caused the Harrod Trust by virtue of a diminution in the value of the shares of stock in TSR.

The Sixth Circuit, in its Opinion, cites the settlement agreement between the Harrod Trust and MDFC and recites that there had been a dispute over the insurance proceeds. However, on the second page of the Settlement Agreement, without mentioning lender liability, the Harrod Trust releases MDFC from all claims (Appendix D).

After TSR filed for bankruptcy protection, the Trustee filed suit in United States Bankruptcy Court for the Western District of Kentucky, seeking to avoid the transfer of the Harrod policy to the Harrod Trust and seeking to recover the $250,000.00 paid to the Harrod Trust. The Bankruptcy Court found that the transfer constituted actual fraud under Kentucky law and ordered it set aside, and the $250,000.00, plus interest, to be paid to the Trustee.

That decision was appealed to United States District Court for the Western District of Kentucky.

The District Judge found that the Bankruptcy Judge's reasoning was wrong, that there was no actual fraud, but that there was constructive fraud, and, therefore, even though the reason was incorrect, the decision should be affirmed.

That decision was appealed to United States Court of Appeals for the Sixth Circuit.

The Circuit Court recognized that in review of bankruptcy decisions, district courts are not the triers of fact, but rather it is the Bankruptcy Court's obligation is to make findings of fact, which are to be accepted, unless clearly erroneous. *In re Batie (Investors Credit Corp. v. Batie)*, 995 F.2d 85 (6th Cir. 1993*); Halbert v. Yousif*, 201 F.3d 774 (6th Cir. 2000*); Key Bank v. Jost*, 136 F.3d 1455 (11th Cir. 1998*)*.

Both the District Judge and the Circuit Court identified the crucial factual question in the case, to-wit whether the insurance policy **had any value** when it was transferred to the Harrod Trust four months before Harrod died. If it had no value, then the creditors of the bankrupt estate were not damaged.

The Circuit Court decision expressed the question in the following language:

> "If Heavrin is correct, and TSR did not lose anything of value when it transferred the Harrod policy to the Trust, then TSR's unsecured creditors were not defrauded and the transfer cannot be avoided. See *Houston v. Edgeworth* (In

> re Edgeworth), 993 F.2d 51, 55-56 (5th Cir. 1993) ("When a payment by the insurer cannot inure to the debtor's pecuniary benefit, then that payment should neither enhance nor decrease the bankruptcy estate."). The fact that the Trust was able to secure a payment from MDFC by virtue of its ownership of the Harrod policy, in other words, does not make the transfer avoidable if TSR would have been unable to extract a similar benefit had it retained ownership of the policy." 422 F.3d 405, 411.

Both the District Court and the Circuit Court proceeded to a decision without considering the fact that **the Bankruptcy Judge never made a finding of fact on the most crucial factual issue in the case.** The Bankruptcy decision focused entirely on the Kentucky law of fraudulent conveyances and never touched on the issue of whether or not the insurance policy had value. The decision assumes that there was value, merely because there was an ownership interest. The inquiry should not have stopped there. Mere ownership does not automatically mean value. *Houston v. Edgeworth, supra.*

Faced with the fact that the Bankruptcy decision did not contain a finding of fact as to value, the case should have been remanded to Bankruptcy Court to hear evidence and make a finding as to whether or not the insurance policy had value when it was transferred.

Moreover, a fully assigned policy is not part of the bankrupt estate. In *Estate of Lellock v. Prudential Insurance Company of America,* 811 F.2d 186 (3d Circuit 1987), and *In re Swartout,* 123 B.R. 794 (Bankr. S. D. Ohio 1991) are cases that deal with assignments that are

identical to the assignment in the case at bar (Appendix E).

In both of those cases the respective courts held that a fully assigned policy was not property of the bankrupt estate.

In the case at bar, the Sixth Circuit held that Heavrin did not 'unconditionally' establish that MDFC was entitled to all of the proceeds of the policy. First, the Circuit Court of Appeals is not a fact-finding court. Secondly, 'unconditionally' establishes a standard of proof that is not recognized in any jurisdiction. Preponderance of the evidence, clear and convincing evidence, and proof beyond a reasonable doubt are the standards of proof that are commonly found in American Jurisprudence. 'Unconditional' proof is a heretofore unknown standard the Sixth Circuit has imposed on the case.

As to the proof TSR believed the policy was fully assigned, the Jackson National Insurance Company believed the policy was fully assigned, MDFC believed the policy was fully assigned, and Heavrin believed the policy was fully assigned when he filed the Claimant's Statement with the insurance company. (Appendix I).

Further, Heavrin attempted to call David Nelson of MDFC, Mike Forrester, the insurance agent who had thirty years experience and prepared the Assignment, and David Cantor, an attorney who specializes in Bankruptcy, to testify that the policy was fully assigned. The Bankruptcy Court would not allow these witnesses to testify and the Sixth Circuit ignored their Avowals. And, while the Sixth Circuit was rendering its fact-based Opinion, the Court never mentions the Assignment, which was introduced as part of Heavrin's case (Appendix

E).

In his addition to the Adversary Proceeding brought by the Trustee, he caused Heavrin to be prosecuted for Bankruptcy Fraud. At the conclusion of a two-week trial, the United States District Court entered a Verdict of Not Guilty on all Counts. In rendering its Verdict, the United States District Court said,

> Most importantly, MDFC had an absolute right to receive the $2,000,000 proceeds of the Policy. No one has suggested a credible legal reason why the entire proceeds were not payable to MDFC. The claims against MDFC by the trust, whatever their basis, are independent of MDFC's right to receive the Policy proceeds. Jackson National sent Heavrin a check made payable to the Harrod Trust after negotiations with MDFC. Whatever the proffered reason for settlement between MDFC and the Harrod Trust, the money was not part of the estate.

The fact that MDFC only gave the Bankrupt TSR $1.75 million in credit is not dispositive of the issue. Originally, MDFC did not give *any* credit to TSR for any of the proceeds of the policy (Appendix H): although it had received payment on November 3, 1994. It was not until several months later, after the Trustee brought an Adversary Proceeding, that MDFC amended its proof of claim to show that it had only received $1.75 million from the insurance policy.

As to the proof of assignment, the contract states unequivocally that the insurance policy is assigned to MDFC and it has ALL rights of ownership (Appendix E)

and, three days before payment was made, Jackson National received a letter from Joel Price, attorney for MDFC, in which he demanded the full-face amount of the policy by virtue of the assignment (Appendix F).

KRS 304.14-250 (Appendix G) provides that life insurance policies can be assigned as collateral for loans, and Kentucky is a UCC state, and under the Uniform Commercial Code assignments of life insurance can be made to collateralize a loan. The Opinion of the Sixth Circuit, therefore, negates the Uniform Commercial Code and the Kentucky Statute.

All of these points illustrate the impropriety of a Circuit Court becoming a fact-finding Court. If the Circuit Court of Appeals had found facts favorable to Heavrin, that would have also been improper. The Appeals Court is not the place for factual determinations.

## REASONS FOR GRANTING THE PETITION

There are four compelling reasons for granting the writ.

First is the obvious one, Petitioner has been denied his day in court. No court has considered all the evidence and made a finding of fact on the one issue which should have decided the case, *id est*, did the fully assigned policy have value to the Estate when ownership was transferred?

Second, it is very dangerous to leave uncorrected a reported decision from one of the Circuit Courts of Appeal, which so clearly disregards the established case law requiring the appellate courts to resist the

temptation to make findings of fact, rather than remand cases and require the proper court to make those findings.

Third, a fully assigned insurance policy is not property of the bankrupt estate.

Fourth, the Kentucky Statutes and the Uniform Commercial Code allow for the assignment of insurance policies to collateralize a loan. The holding of the Sixth Circuit negates the Kentucky Statute and the UCC. Regardless of the clarity of an assignment, no lender will ever be sure an assignment is valid.

## CONCLUSION

For the foregoing reasons, the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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No. 04-5297

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

In Re: TRIPLE S RESTAURANTS, INC.,
Debtor,

J. BAXTER SCHILLING, Trustee,
Appellee,

v.

DONALD M. HEAVRIN,
Appellant.

May 31, 2005, Argued

August 30, 2005, Decided

August 30, 2005, Filed

COUNSEL: ARGUED: James A. Earhart, Louisville, Kentucky, for Appellant.

J. Baxter Schilling, Louisville, Kentucky, for Appellee.

ON BRIEF: James A. Earhart, Louisville, Kentucky, for Appellant.

J. Baxter Schilling, Louisville, Kentucky, for Appellee.

JUDGES: Before: BOGGS, Chief Judge; GILMAN, Circuit Judge; and CLELAND, District Judge. *

OPINION BY: RONALD LEE GILMAN

OPINION:

RONALD LEE GILMAN, Circuit Judge. Donald M. Heavrin appeals from the judgment of the district court, which affirmed a decision of the bankruptcy court permitting J. Baxter Schilling, the Trustee for Triple S Restaurants (TSR), to avoid the fraudulent transfer of a life insurance policy and to recover the value of the transfer on behalf of TSR's creditors. The policy on the life of Heavrin's stepfather, Robert Harrod, was transferred from TSR to a trust benefitting Heavrin and his stepsister, Bobbie Bridges, shortly before TSR filed for bankruptcy. When the bankruptcy court determined that the transfer could be avoided, Heavrin and Bridges were ordered to pay the TSR Trustee the $ 250,000 that they had received from the insurance carrier, plus interest. The district court affirmed this decision, as well as the bankruptcy court's denial of the motion that Heavrin filed seeking to recuse the bankruptcy court judge.

On appeal, Heavrin argues that the transfer was not fraudulent because all of the proceeds from the life insurance policy had previously been assigned by TSR to the McDonnell Douglas Finance Corporation (MDFC), one of TSR's creditors, and therefore the policy was of no value to either TSR or the Trust. He also claims that the payment from MDFC, which he received through the Trust, was in settlement of unrelated lender-liability claims that Harrod's estate had against MDFC. For the reasons set forth below, we AFFIRM the judgment of the district court.

I. BACKGROUND

A. Factual background

In 1988, Michael Macatee and Robert Harrod formed TSR to obtain a franchise for the operation of Sizzler restaurants in Louisville, Kentucky. Each of them owned 50% of TSR's stock. Heavrin, a Kentucky lawyer who was Harrod's stepson, served as TSR's attorney.

Prior to the formation of TSR, negotiations regarding a loan had taken place between MDFC and S&B of Indiana, Inc., a predecessor in interest of TSR. The terms of a December 1987 commitment letter issued to S&B by MDFC required "Robert E. Harrod and Michael R. Macatee . . . to obtain Key Man Life Insurance in the minimum amount of $ 3,560,000.00 naming MDFC Equipment Leasing Corporation as beneficiary." When the loan agreement was actually executed three months later, in March of 1988, TSR was substituted for S&B. Harrod, Macatee, and TSR were all co-signers on the $ 3.56 million loan from MDFC, for which all three were jointly and severally liable.

Three days after securing the loan from MDFC, S&B purchased an insurance policy on Harrod's life from Transamerica Occidental Life in the amount of $ 2 million. S&B then transferred all of its interest in the Harrod policy to TSR. (Four policies were also obtained on the life of Macatee, each in the amount of $ 500,000, although the details regarding these policies are not reflected in the record.) In November 1991, the Harrod policy from Transamerica was replaced by a $ 2 million policy issued by Jackson National. TSR made this substitution in order to save money on the premium payments for the Harrod policy. Shortly after

the Transamerica policy was replaced by the Jackson National policy, Michael Forrester, an insurance agent and friend of Heavrin, completed a collateral assignment of the Harrod policy proceeds from TSR to MDFC.

Harrod and Macatee informed Heavrin in August of 1992 that TSR was in dire financial straits and that they wanted TSR to file a Chapter 11 bankruptcy petition. Heavrin advised them against filing for bankruptcy, instead counseling them to attempt to reach an arrangement with TSR's creditors that would enable TSR to remain in business. Less than a month later, a lawyer who shared office space with Heavrin drafted an irrevocable trust agreement (the Trust) in which Harrod was the grantor and trustee. The beneficiaries of the Trust were Heavrin and Bridges. Harrod transferred his 500 shares of TSR stock to the Trust in September of 1992.

TSR's financial condition continued to deteriorate, and, by November of 1993, it did not have the resources to make the quarterly premium payments on the Harrod policy. As a result, MDFC began to pay the premiums to ensure that the policy would not lapse. Making certain that the premium payments were submitted promptly became even more crucial in March of 1994, when MDFC was informed that Harrod had been diagnosed with lung cancer.

In June of 1994, Heavrin told MDFC that Harrod's cancer was terminal. Shortly thereafter, TSR transferred its ownership of the Harrod policy to the Trust without receiving any financial consideration. This transfer was executed on TSR's behalf by

Macatee. At the time of the transfer, TSR owed hundreds of thousands of dollars in outstanding unsecured debts and was insolvent.

Three days after the Trust became the owner of the Harrod policy, Heavrin began negotiating with MDFC for a settlement on behalf of the Trust. On September 2, 1994, while these negotiations were ongoing, Harrod died. MDFC and Heavrin signed a settlement agreement a month later, on November 3, 1994. In accordance with this agreement, MDFC, as the beneficiary of the policy, instructed Jackson National to pay $ 250,000 of the proceeds to the Trust. Jackson National subsequently paid the Trust the $ 250,000 plus a small amount of post-death interest as required by the policy. Although Heavrin and Bridges were equal beneficiaries of the Trust, they apparently agreed that Bridges would receive $ 75,000 and that Heavrin would keep the remainder.

B. Bankruptcy court proceedings

In September of 1994, TSR filed for bankruptcy protection. MDFC filed a proof of claim against TSR for $ 3,304,165.63 two months later. No mention is made in this document of the $ 2 million in life insurance proceeds that were paid as a result of Harrod's death. At oral argument, however, counsel for Heavrin acknowledged that MDFC eventually credited TSR for the $ 1.75 million payment that MDFC received from the proceeds of the Harrod policy. But MDFC did not credit TSR for the entire $ 2 million of the policy proceeds, presumably because it subtracted the $ 250,000 payment that it directed Jackson National to pay to the Trust.

In July of 1996, the Trustee for TSR filed suit in the United States Bankruptcy Court for the Western District of Kentucky, seeking to avoid the transfer of the Harrod policy to the Trust under 11 U.S.C. §§ 544(b) and 548(a), and to recover the $ 250,000 plus interest paid to the Trust by Jackson National. The TSR Trustee alleged that the payment directed by MDFC to the Harrod Trust was facilitated by the Trust's ownership of the Harrod policy. Heavrin insisted, however, that the payment was in settlement of certain lender-liability claims that he had considered bringing against MDFC on behalf of Harrod's estate.

The bankruptcy court ordered the avoidance of the transfer under 11 U.S.C. §§ 544(b) and 548(a) on the grounds that the transfer was made without valuable consideration and with the intent to defraud TSR's creditors. Pursuant to 11 U.S.C. § 550(a), which permits a trustee to recover the property or the value of the property whose transfer was avoided under § 544 or § 548, the bankruptcy court held that the payment from Jackson National to the Trust was recoverable by the Trustee for the benefit of TSR and its creditors. Heavrin and Bridges were therefore ordered to pay the TSR Trustee the money that they had received through the Harrod Trust, together with interest at 8% per annum.

The bankruptcy court also directed Heavrin to disgorge approximately $ 46,000 of the roughly $ 153,000 in attorney fees that he was paid by TSR during the year preceding TSR's bankruptcy because Heavrin had failed to report these payments to the bankruptcy court as required by the Federal Bankruptcy Rules. *See* 11 U.S.C. § 329; Fed. R. Bankr. P. 2016. Finally, the

bankruptcy court denied Heavrin's petition requesting that Bankruptcy Judge David T. Stosberg recuse himself on the grounds of his alleged bias against Heavrin.

C. District court proceedings

Heavrin appealed the bankruptcy court's decision to the United States District Court for the Western District of Kentucky. The district court upheld the decision of the bankruptcy court with respect to the avoidance of the transfer, but did so under a different theory. It held that the transfer was avoidable under 11 U.S.C. § 548(a) on the basis of constructive fraud rather than actual fraud. The district court also upheld the denial by the bankruptcy court of Heavrin's recusal motion, but concluded that the bankruptcy court had erred in requiring Heavrin to disgorge approximately $ 46,000 of the attorney fees that he had received from TSR prior to the bankruptcy.

Heavrin timely appealed to this court, claiming that the district court had erred in affirming the avoidance of the transfer to the Trust and in upholding the bankruptcy court's denial of his recusal motion. He also argues, apparently for the first time, that the bankruptcy court erred in requiring him to pay prejudgment interest at a rate of 8% per annum on the attorney fees that he was ordered to disgorge.

D. Other appeals

Two previous appeals have been heard by this court in connection with the TSR bankruptcy. In *Schilling v. Heavrin (In re Triple S Restaurants, Inc.)*, 131 Fed.

Appx. 486, 2005 WL 1140625 (6th Cir. 2005) (unpublished) (per curiam) [hereinafter *TSR I*], we affirmed the bankruptcy court's denials of motions submitted by Heavrin, Bridges, and the Trust to recuse Bankruptcy Judge Stosberg, to extend the time to appeal, and to permit amendment of the notice of appeal to include the Trust and Bridges as appellants. We also affirmed the district court's finding that the bankruptcy court's order was a final judgment. In *Schilling. v. Heavrin (In re Triple S Rests., Inc.)*, 130 Fed. Appx. 766, 2005 WL 1109615 (6th Cir. 2005) (unpublished) (per curiam) [hereinafter *TSR II*], we reinstated the bankruptcy court's judgment requiring Heavrin to disgorge a portion of the attorney fees that he received from TSR prior to the bankruptcy.

## II. ANALYSIS

### A. Standard of review

"When we review bankruptcy decisions, our standard of review is slightly different from our normal standard of review because district courts are not the triers of fact of bankruptcy cases." *Investors Credit Corp. v. Batie (In re Batie)*, 995 F.2d 85, 88 (6th Cir. 1993). Because the bankruptcy court makes the initial findings of fact, the district court is bound by these findings unless they are clearly erroneous. *Id.* "If the district court's decision is appealed to this court, then we review the district court's conclusions of law de novo," and we accord no deference to the district court's findings of fact. *Id.* (stating that "we do not review the district court's assessment of the bankruptcy court's factual findings," but instead "follow the *bankruptcy* court's factual

findings . . . [unless] we consider them to be clearly erroneous") (emphasis in original).

B. Avoidance of the transfer

The bankruptcy court determined that the transfer of the Harrod policy from TSR to the Trust could be avoided by the TSR Trustee in accordance with either 11 U.S.C. § 544(b) or 11 U.S.C. § 548(a). Pursuant to section § 544(b), a trustee may avoid a transfer if the transferor was insolvent at the time and if the transfer is voidable under applicable state law. There is no dispute in the present case that TSR was insolvent at the time of the transfer. Thus, the dispositive question under § 544(b) is whether the transfer is voidable under Kentucky law. The bankruptcy court held that the transfer of the Harrod policy is voidable under Kentucky Revised Statutes § 378.010, which provides that transfers shall be void as to creditors if "made with the intent to delay, hinder or defraud creditors, purchasers or other persons," and under Kentucky Revised Statutes § 378.020, which provides that transfers of a debtor shall be void against existing creditors if made "without valuable consideration."

In an alternative holding, the bankruptcy court also determined that the transfer of the Harrod policy could be avoided by the TSR Trustee pursuant to 11 U.S.C. § 548(a). This section permits the avoidance of a transfer made within one year of the filing of the bankruptcy petition if the transfer was made with the intent to hinder, delay, or defraud the transferor's existing or future creditors, or if the transferor was insolvent at the time of the transfer and did not receive

consideration that was reasonably equivalent in value to the transferred asset.

Heavrin argues that the bankruptcy court erred in concluding that the transfer was avoidable under either §§ 544(b) or 548(a) because, he asserts, the ownership of the Harrod policy had no value for TSR. As a result, transferring the policy to the Trust purportedly did not diminish the bankruptcy estate. He insists that (1) the Harrod policy proceeds were not the property of TSR because they were fully assigned to MDFC, and (2) the $ 250,000 payment directed by MDFC to the Trust was in settlement of certain lender-liability claims possessed by Harrod that were completely unrelated to the Trust's ownership of the Harrod policy.

*1. Heavrin has not established that MDFC was unconditionally entitled to all of the policy proceeds*

If Heavrin is correct, and TSR did not lose anything of value when it transferred the Harrod policy to the Trust, then TSR's unsecured creditors were not defrauded and the transfer cannot be avoided. *See Houston v. Edgeworth (In re Edgeworth)*, 993 F.2d 51, 55-56 (5th Cir. 1993) ("When a payment by the insurer cannot inure to the debtor's pecuniary benefit, then that payment should neither enhance nor decrease the bankruptcy estate."). The fact that the Trust was able to secure a payment from MDFC by virtue of its ownership of the Harrod policy, in other words, does not make the transfer avoidable if TSR would have been unable to extract a similar benefit had it retained ownership of the policy.

Heavrin's first contention--that no transfer of TSR's property occurred because the Harrod policy proceeds were fully assigned to MDFC--is not borne out by the evidence. Heavrin insists that, because TSR had assigned the proceeds of the Harrod policy to MDFC, the entire $ 2 million from Jackson National belonged to MDFC regardless of whether TSR retained ownership of the policy or transferred ownership to the Trust. *See Edgeworth*, 993 F.2d at 55 ("Acknowledging that the debtor owns the policy, however, does not end the inquiry. The question is not who owns the policy, but who owns the liability proceeds.") (citation and quotation marks omitted).

Whether MDFC was unconditionally entitled to the full proceeds of the Harrod policy, however, is far from clear. The TSR Trustee points to the fact that there are no documents demonstrating that the assignment of the Harrod policy was collateral for the loan from MDFC. In the absence of such proof, the Trustee asserts that the issue was ripe for negotiation and litigation--proceedings that could have resulted in TSR retaining at least a part of the Harrod policy proceeds.*See Demczyk v. Mutual Life Ins. Co. (In re Graham Square)*, 126 F.3d 823, 831 (6th Cir.1997) (stating that 'property of the estate includes the debtor's interest in a cause of action").

Circumstantial evidence, admittedly, supports Heavrin's contention that all of the Harrod policy proceeds belonged to MDFC as collateral for the loan to TSR. For instance, three days after securing the loan from MDFC, TSR's predecessor in interest, S&B, purchased the original policy on Harrod's life from Transamerica. An internal MDFC memorandum also

states that MDFC's loan to TSR was "secured by a lien on the equipment in the stores it financed, a letter of credit in the amount of $ 356K, and a key man insurance policy on the partners in the amount of $ 2,000K."

On the other hand, there is no direct evidence to establish that MDFC was entitled to *all* of the proceeds from the Harrod policy. The policy is not mentioned in any of the loan documents between MDFC and TSR. And, although the policy on Harrod's life was purchased three days after the loan was made, the assignment of the policy proceeds to MDFC did not take place until November of 1991, more than three years later.

There is also evidence that TSR had intended another use for at least some of the Harrod policy proceeds. A stock purchase agreement entered into by Harrod and TSR in 1988 states that, upon Harrod's death, the "proceeds of the life insurance policy(s) pertaining to this Agreement shall be used for the purpose of redemption." The insurance policy referenced in the agreement is the Jackson National policy on Harrod's life. This potential dual use of the proceeds--for both loan repayment and stock redemption--creates an obvious ambiguity.

Finally, the facts support another theory under which TSR would be entitled to some of the insurance proceeds without resorting to extortionate litigation tactics. TSR's $ 3.56 million loan was secured by $ 4 million worth of life insurance--$ 2 million on the life of Harrod and $ 2 million on the life of Macatee. Thus, although MDFC was theoretically entitled to collect up to $ 2 million upon the death of either man, a proportional division of liability would result in

approximately $ 1.75 million being applied to MDFC's loan and leave roughly $ 250,000 to the owner of the policy. This is precisely the amount that Heavrin gained through the transfer of the policy from TSR to the Trust, an amount that presumably would have redounded to TSR in the absence of the transfer.

Although the record is ambiguous as to *why* MDFC ceded $ 250,000 to the Trust, there is no question that the settlement agreement between the Trust and MDFC acknowledges that "subsequent to the Trust becoming the beneficiary of the Policy, a dispute had arisen between the Trust and MDFC as to the amount of the Policy proceeds payable to MDFC." In order to "settle the dispute in a manner which [would] expedite payment of the Policy proceeds," MDFC agreed to pay the Trust $ 250,000 plus interest. This evidence severely weakens Heavrin's assertion that the entire proceeds of the Harrod policy undisputably belonged to MDFC and consequently were of no value to TSR. We therefore cannot say that the bankruptcy court erred when it rejected Heavrin's claim on this basis.

Heavrin's contention that all of the Harrod policy proceeds belonged to MDFC is further undercut by an argument in Heavrin's appellate brief. He contends that, regardless of whether TSR retained ownership of the Harrod policy or transferred it to the Trust, TSR was entitled to "$ 2,000,000 in debt reduction upon payment of all the Policy proceeds to MDFC." But Heavrin's counsel acknowledged at oral argument that, in the proof-of-claim documents that MDFC filed in the TSR bankruptcy proceedings, MDFC credited TSR with only $ 1.75 million in debt reduction after receiving that amount from the proceeds from the Harrod policy.

This amount is $ 250,000 shy of the full $ 2 million in policy proceeds payable on Harrod's death, and corresponds to the allocation of the proceeds that Heavrin negotiated on behalf of the Trust. The fact that MDFC credited TSR for only a portion of the proceeds of the Harrod policy is an indication that MDFC did not consider all of the proceeds to be its property.

Furthermore, even if the primary effect of avoidance would be to send the $ 250,000 back to MDFC, that money would offset TSR's outstanding debt to MDFC, thereby freeing up funds in that amount to pay the unsecured creditors. Avoiding the $ 250,000 transfer, in other words, decreases the amount of secured debt and increases the Trustee's ability to pay the remaining creditors. Because such avoidance establishes a benefit to TSR's unsecured creditors, we can--and do--reject Heavrin's argument that avoiding the transfer would benefit only MDFC.

*2. Heavrin has not established that the payment from MDFC was in settlement of lender-liability claims*

Heavrin also advances the argument that the transfer of the Harrod policy to the Trust did not harm TSR's unsecured creditors because the payment that the Trust received from MDFC was in settlement of certain lender-liability claims possessed by Harrod that were completely unrelated to the Trust's ownership of the Harrod policy. He contends that MDFC had the settlement to the Trust paid from the proceeds of the Harrod policy merely as a matter of convenience, not because the policy proceeds were in any way related to the payment.

The circumstances surrounding the payment from MDFC, however, do not support Heavrin's contention on this ground either. As the bankruptcy court noted, a letter written to Heavrin by MDFC states that "the disbursement of the $ 250,000 would represent the full settlement of all matters relating to this insurance policy." This letter alone constitutes persuasive evidence that the payment authorized by MDFC was related to the Trust's ownership of the Harrod policy. Moreover, the settlement was paid to the Trust, not to Harrod's estate. If the $ 250,000 payment authorized by MDFC was in settlement of lender-liability claims that Harrod possessed personally, as Heavrin argues, then MDFC would presumably have directed the payment to Harrod's estate. The fact that this was not done suggests that ownership of the Harrod policy, which the Trust possessed but Harrod's estate did not, was an important consideration for MDFC in authorizing the payment to the Trust.

Also problematic for Heavrin is the fact that the payment by MDFC came directly out of the Harrod policy proceeds as a transfer of funds from Jackson National to the Trust. Heavrin explains that he arranged for this payment to be made in this manner in response to his "fear[] that MDFC would renege on the settlement after it received the Policy proceeds." But this admission suggests that the owner of the Harrod policy had at least some additional leverage when negotiating with MDFC, which is contrary to Heavrin's argument that ownership of the policy was "essentially meaningless and absolutely worthless."

The core of Heavrin's argument is that he asserted lender-liability claims on behalf of Harrod's estate and

that he collected the $ 250,000 as a result of those claims. The bankruptcy court rejected this argument, observing that the Trust did not stand in a borrower-lender relationship with MDFC and finding that Heavrin had not pointed to any egregious conduct by MDFC that could have formed the basis for such claims. Although we agree with the bankruptcy court's observation that the Trust did not stand in a borrower-lender relationship with MDFC, Heavrin has a legitimate argument to the extent that he was negotiating on behalf of Harrod's estate rather than the Trust. Nevertheless, Heavrin's consistent failure to explain the legal basis for the alleged lender-liability claims is fatal to his defense.

Heavrin does not insist that he is prevented from making such a disclosure by any confidentiality agreement with MDFC. And the disclosure of any grounds possessed by Harrod for such a suit could not possibly harm MDFC because the litigation between the Trustee and MDFC has already been settled. *See Schilling v. MDFC Equip. Leasing Corp.*, AP No. 95-3096 (Bankr.W.D. Ky. Dec. 11, 1995) (unpublished) (stating that the agreed-upon order was entered in "settlement and compromise of any and all causes of action of plaintiff and/or this bankruptcy estate against defendant"). Heavrin's inability to provide a description of the alleged lender-liability claims suggests that there were no such claims. Instead, the Trust's ownership of the Harrod policy appears to have been the key factor that caused MFDC to have the $ 250,000 paid to the Trust. We therefore agree with the bankruptcy court that Heavrin has failed to establish that the policy proceeds paid to the Trust were in settlement of any lender-liability claims.

In agreeing with the courts below regarding Heavrin's inability to explain the nature of the alleged claims, we also affirm those courts' decision to shift the burden of proof to Heavrin on this point. Indeed, Heavrin does not argue that he presented evidence that justified a contrary finding as to the lender-liability claims, but instead maintains that the bankruptcy court erred in shifting the burden of proof to him to do so. He contends that the TSR Trustee had the burden to demonstrate that the policy proceeds paid to the Trust were made to settle claims that would have rightfully belonged to TSR had it retained ownership of the Harrod policy. This is the contention to which we now turn.

*3. Heavrin's position as an insider and his status as a close relative constitute "badges of fraud" that justify shifting the burden of proof*

Heavrin is correct in pointing out that a trustee attempting to avoid an allegedly fraudulent transfer normally bears the burden of proof on that issue, but the bankruptcy court in the present case found that the transfer of the Harrod policy from TSR to the Trust displayed several "badges of fraud" that justified shifting the burden of proof to Heavrin to demonstrate that the transfer did not harm TSR's unsecured creditors. See *United States v. Westley*, 7 Fed. Appx. 393, 2001 WL 302068, at *6 (6th Cir. 2001) (unpublished) ("If there are 'badges of fraud' which cast suspicion on the transaction, the burden of proof shifts to the defendant to explain the transaction and show that it was not fraudulent."). "Badges of fraud are circumstances so frequently attending fraudulent transfers that an inference of fraud arises from them."

*United States v. Isaac*, 1992 U.S. App. LEXIS 16657, No. 91-5830, 1992 WL 159795, at *4 (6th Cir. July 10, 1992) (unpublished) (citation and quotation marks omitted).

One badge of fraud identified by the bankruptcy court with respect to the transfer of the Harrod policy was that the beneficiaries of the Trust--Heavrin and Bridges--were the children of one the co-owners of TSR. *See Isaac*, 1992 U.S. App. LEXIS 16657, 1992 WL 159795, at *4 (stating that "Kentucky courts treat transfers between close family members or people in confidential relationships, in the context of impending financial difficulties, as a badge of fraud"); *Cooper v. Osbourne (In re Osbourne)*, 124 B.R. 726, 728 (Bankr. W.D. Ky. 1989) (listing "transfers made to a family member or close relation" as a badge of fraud).

Another badge of fraud identified by the bankruptcy court was Heavrin's position as corporate counsel for TSR, which made him an insider with respect to TSR's transfer of the Harrod policy to the Trust. Because he benefitted from the transfer, the court found that Heavrin's insider status was a badge of fraud that justified shifting the burden of proof. *See Isaac*, 1992 U.S. App. LEXIS 16657, 1992 WL 159795, at *4 ("We have often written that courts look with suspicion upon transactions between persons occupying confidential relations. When such a transaction is exposed to scrutiny, the burden is always upon the recipient of the property acquired to show that the conveyance was fairly made and not tainted with an intent to accomplish a fraudulent purpose.") (citation and quotation marks omitted).

In shifting the burden of proof to Heavrin after finding that the transfer of the Harrod policy was attended by badges of fraud, the bankruptcy court cited to *Green v. Stevenson (In re Stevenson)*, 69 B.R. 49 (Bankr. E.D. Mo. 1986), for support. The court in *Stevenson*, however, decided to shift the burden of proof to the defendant only after concluding that the transfer at issue was made without adequate consideration. *Id.* at 50 ("Where a transfer is between related parties, the transfer is subject to close scrutiny and gives rise to a presumption of actual fraudulent intent where the transfer is without adequate consideration.") (citation and quotation marks omitted); *see also* Peter Spero, *Fraudulent Transfers: Applications and Implications* § 15:3 (2005) ("Where the transaction involves family members . . . *and the transaction was made without any tangible consideration*, a heavier burden is placed upon the grantee to demonstrate fair consideration for the transfer.") (citation and quotation marks omitted) (emphasis added).

In the present case, the parties dispute whether the Trust provided adequate consideration for the transfer of the Harrod policy. The TSR Trustee argues that the Trust provided no consideration. Heavrin, on the other hand, contends that the Trust's diligence in having MDFC keep up the premium payments was adequate consideration. The bankruptcy court resolved this dispute by concluding that the consideration received by TSR for the transfer was inadequate, but we need not reach this issue in order to affirm the district court's finding that the transfer may be avoided pursuant to 11 U.S.C. § 548(a). We also do not have to reach the issue in order to decide whether the bankruptcy court erred in shifting the burden of proof

on this issue to Heavrin, because we hold that the burden of proof may shift even where consideration has not been shown to be inadequate. Our holding is based on a survey of the limited caselaw on this issue and a consideration of the purposes served by shifting the burden of proof when badges of fraud are shown.

In *Westley*, 7 Fed. Appx. 393, 2001 WL 302068, at *6, this court concluded that the fact that insiders were the beneficiaries of the transfer was a "badge of fraud" that, in and of itself, "cast suspicion on the transaction" and shifted the burden of proof to the defendants. *See also Anderson & Assocs. PA v. S. Textile Knitters De Honduras Sewing Inc. (In re S. Textile Knitters)*, 65 Fed. Appx. 426, 2003 WL 124771, at *6 (4th Cir. 2003) (unpublished) ("Since the transfers at issue here were made to members of the family, Defendants have the burden to establish both a valuable consideration and the bona fides of the transaction by clear and convincing testimony."). The above-referenced treatise, *Fraudulent Transfers: Applications and Implications*, also acknowledges that, where a transfer is made to an insider, "the burden may change . . . [if] the evidentiary facts as to the nature and value of the consideration are within the transferee's control, in which case the burden of coming forward with evidence on the fairness of the consideration shifts to the transferee." § 15:3 (citation and quotation marks omitted).

MDFC's true reason for directing the $ 250,000 payment to the Trust is unclear. This enigma is due in part to the fact that Heavrin, as the chief negotiator of the deal with MDFC, offered very little evidence with respect to why the Trust received the money. The assignment of the burden of proof thus becomes the key

to determining whether the transfer of the Harrod policy may be avoided. Given the badges of fraud attending to the transaction--revolving around the fact that the lawyer for the failing business was the stepson of one of its founders and the primary beneficiary of the transfer—we find no good reason to require the Trustee to produce evidence that could much more readily be supplied by Heavrin. Under such circumstances, equitable principles call upon Heavrin to demonstrate that the transfer of the insurance policy did not harm TSR's unsecured creditors. *See Doss v. Green (In re Green)*, 986 F.2d 145, 150 (6th Cir. 1993) ("This court marvels at the debtor's attempt to circumvent the fraudulent conveyance laws. However, bankruptcy courts are courts of equity. A court of equity will not relieve a party with 'unclean hands.' This doctrine closes the doors of a court of equity to one tainted with inequitableness or bad faith relative to the matter in which he seeks relief.") (citations and quotation marks omitted).

Heavrin has failed to demonstrate that the transfer of the Harrod policy to the Trust did not harm TSR's unsecured creditors. We therefore conclude that the bankruptcy court did not err in determining that the transfer of the policy could be avoided pursuant to 11 U.S.C. § 548(a), which permits the avoidance of a transfer if it was made with the intent to hinder, delay, or defraud a transferor's existing and future creditors. *See Zentek GBV Fund IV, LLC v. Vesper*, 19 Fed. Appx. 238, 2001 WL 1042217, at *5 (6th Cir. 2001) (unpublished) ("'Because proof of actual intent to hinder, delay or defraud creditors may rarely be established by direct evidence, courts infer fraudulent intent from the circumstances surrounding the

transfer.'") (quoting *Brown v. Third Nat'l Bank (In re Sherman)*, 67 F.3d 1348, 1353 (8th Cir. 1995)).

B. Assessment of prejudgment interest

Heavrin raises, for the first time on appeal, the contention that the bankruptcy court erred in imposing prejudgment interest on the roughly $ 46,000 in attorney fees that he was required to disgorge. He did not list this as one of the issues to be appealed from the bankruptcy court and did not raise the issue before the district court. The issue is therefore waived. *See United States v. Ninety-Three Firearms*, 330 F.3d 414, 424 (6th Cir. 2003) ("This court has repeatedly held that it will not consider arguments raised for the first time on appeal unless our failure to consider the issue will result in a plain miscarriage of justice.") (citation and quotation marks omitted).

Even if this claim had not been waived, however, it would have no merit. As Heavrin concedes, the assessment of prejudgment interest is left to the sound discretion of the bankruptcy court. Heavrin was paid over $ 153,000 in attorney fees by TSR in the year preceding TSR's filing for bankruptcy, and the bankruptcy court required Heavrin to disgorge less than a third of this amount. This court reviewed the bankruptcy court's partial disgorgement order in *TSR II*, 130 Fed. Appx. 766, 2005 WL 1109615, at *6 (6th Cir. 2005) (unpublished) (per curiam), and concluded that the bankruptcy court's "final order was, if anything, unduly generous to Heavrin." Thus we cannot say that the bankruptcy court abused its discretion in imposing prejudgment interest at a rate of 8% per annum on the approximately $ 46,000 in attorney fees that Heavrin

was required to disgorge. *See Henderson v. Kisseberth (In re Kisseberth)*, 273 F.3d 714, 720 (6th Cir. 2001) (stating that the court "will find an abuse of discretion only upon a definite and firm conviction that the trial court committed a clear error of judgment") (citation and quotation marks omitted).

C. Recusal of the bankruptcy judge

The final issue raised on appeal is whether Bankruptcy Judge Stosberg erred in not recusing himself. This court partially addressed the issue in *TSR I*, 131 Fed. Appx. 486, 2005 WL 1140625 (6th Cir. 2005) (unpublished) (per curiam), when we reviewed the bankruptcy court's denial of a motion for recusal originally filed by Heavrin in 1995. We affirmed the bankruptcy court's order denying Heavrin's motion because it was not timely. 131 Fed. Appx. 486, [WL] at *1 ("As the bankruptcy court found, the defendants' motion to recuse was untimely and was therefore properly denied."). But Heavrin filed a second recusal motion in 2001 that was based on events occurring after his 1995 motion was filed. This second motion was denied by the bankruptcy court on the merits, with no mention made of untimeliness. In the present appeal, we are therefore bound by the decision of this court in *TSR I* with respect to all arguments raised in Heavrin's 1995 recusal motion, but we reach the merits of the arguments that Heavrin raises in his 2001 motion.

We will uphold a lower court's denial of a recusal motion so long as the court's decision does not constitute an abuse of discretion. *Youn v. Track, Inc.*, 324 F.3d 409, 422 (6th Cir. 2003).The relevant federal

recusal statute, 28 U.S.C. § 455, provides in pertinent part as follows:

> (a) Any justice, judge, or magistrate judge of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.
>
> (b) He shall also disqualify himself in the following circumstances: (1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding . . . .

A judge's unfavorable disposition toward an individual or his case, however, does not typically constitute judicial "bias or prejudice." *See Liteky v. United States*, 510 U.S. 540, 550, 127 L. Ed. 2d 474, 114 S. Ct. 1147 (1994). Rather, "the words [bias and prejudice] connote a favorable or unfavorable disposition or opinion that is somehow *wrongful* or *inappropriate*, either because it is undeserved, or because it rests upon knowledge that the subject ought not to possess . . . or because it is excessive in degree."*Id.* (emphasis in original). Bias on the part of a judge commonly stems from an "extrajudicial" source, meaning knowledge that the judge has acquired that is not based on either the proceedings before him or on other legal proceedings involving the same parties. *Id.* at 551.

In rare cases, a "favorable or unfavorable predisposition can also deserve to be characterized as 'bias' or 'prejudice' because, even though it springs from the facts adduced or the events occurring at trial, it is so

extreme as to display clear inability to render fair judgment." *Id.* These rare cases aside, however, opinions held by judges as a result of what they learn in the proceedings at issue or in earlier proceedings are "not subject to deprecatory characterization as 'bias' or 'prejudice.'" *Id.* ("It has long been regarded as normal and proper for a judge to sit in the same case upon its remand, and to sit in successive trials involving the same defendant.").

Heavrin alleges that Bankruptcy Judge Stosberg was biased against him because of dealings that the two of them had prior to Stosberg's appointment to the bench, during which Heavrin opposed the payment of $ 1,400 in fees to then-examiner Stosberg on the basis that Stosberg's examination was "incompetent, incomplete, and worthless." This dispute was resolved by the federal district court when the debtor was ordered to pay Stosberg's fee over the objection of Heavrin. Although the characterization by Heavrin of Stosberg's work as "incompetent, incomplete, and worthless" might have offended or angered Stosberg at the time, Heavrin's opposition to the payment of the fees was ultimately unsuccessful, and Bankruptcy Judge Stosberg suffered no pecuniary loss as a result. We thus have no reason to believe that Bankruptcy Judge Stosberg remained so upset by Heavrin's past opposition to his fee request that he was unable to decide this case on the merits.

Heavrin further contends that Bankruptcy Judge Stosberg became biased against him as a result of events that occurred during the TSR bankruptcy proceedings. The bankruptcy court imposed sanctions against David Chinn, a bankruptcy attorney hired by

TSR and a tenant in Heavrin's offices, for paying Heavrin a portion of Chinn's retainer from TSR as a rent payment. Heavrin was criticized by the court for accepting the payment in light of his status as a TSR insider and because he had referred the case to Chinn. In its opinion, the bankruptcy court described Heavrin's conduct and characterized his behavior as "deplorable," but then struck these comments from its modified opinion after Heavrin objected. This characterization of Heavrin's behavior, however, was an opinion formed by the bankruptcy court during the proceedings involving Heavrin, and can therefore be deemed an indicium of bias only if it is "so extreme as to display clear inability to render fair judgment." *Liteky*, 510 U.S. at 551. The bankruptcy court removed the offending language from its opinion at Heavrin's request, which leads us to conclude that the court's conduct was not so extreme as to require recusal.

Finally, Heavrin contends that Bankruptcy Judge Stosberg exhibited bias by deciding to place the burden on Heavrin to prove that he was entitled to retain the money paid to him by the Trust, rather than on the TSR Trustee to prove that the transfer should be avoided. According to Heavrin, the "trial was little more than a means to an inevitable end, during the course of which the court was openly hostile to counsel and his client." This argument is without merit not only because we find that the bankruptcy court properly placed the burden of proof on Heavrin, but because Heavrin has failed to produce any concrete examples that demonstrate Bankruptcy Judge Stosberg's alleged hostility. *See General Aviation v. Cessna Aircraft Co.*, 915 F.2d 1038, 1043 (6th Cir.1990) (requiring the moving party to allege "facts which a reasonable person

would believe would indicate a judge has a personal bias against the moving party. Conclusions, rumors, beliefs, and opinions are not sufficient to form a basis for disqualification.") (citations and quotation marks omitted).

None of Heavrin's three complaints regarding Bankruptcy Judge Stosberg give rise to the necessary "definite and firm conviction that the trial court committed a clear error of judgment." *Youn*, 324 F.3d at 422 (citation and quotation marks omitted). We therefore conclude that the bankruptcy court did not abuse its discretion by denying Heavrin's motion to recuse.

## III. CONCLUSION

For all of the reasons set forth above, we AFFIRM the judgment of the district court.

* The Honorable Robert H. Cleland, United States District Judge for the Eastern District of Michigan, sitting by designation.

CIVIL ACTION NO. 3:03CV-217-H, CIVIL ACTION NO. 3:03CV-396-H, CIVIL ACTION NO. 3:03CV-546-H

UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF KENTUCKY

IN RE: TRIPLE S RESTAURANTS, INC.;
DONALD M. HEAVRIN,
PLAINTIFF

v.

J. BAXTER SCHILLING,
DEFENDANT;

J. BAXTER SCHILLING,
PLAINTIFF

v.

ROBERT E. HARROD,
DEFENDANT;

J. BAXTER SCHILLING,
PLAINTIFF

v.

ROBERT E. HARROD, et al.,
DEFENDANTS

February 23, 2004, Decided
February 25, 2004, Entered

JUDGES: JOHN G. HEYBURN II, CHIEF JUDGE, U.S. DISTRICT JUDGE.

OPINION BY: JOHN G. HEYBURN II

OPINION:

**MEMORANDUM OPINION**

This Memorandum Opinion concerns three separate appeals arising out of Triple S Restaurants, Inc. ("TSR") bankruptcy. Each of these appeals is related. Some of the issues raised in each are the same, others are distinct. In addition, the Court is considering another related case on remand from the Sixth Circuit, *United States of America v. Donald M. Heavrin*, Criminal Action No. 3:99CR-113-H. Contemporaneously, the Court is issuing an opinion in that case and makes reference to it here.

In these appeals the Court will consider the following issues in turn: (1) whether the Bankruptcy Court erred by determining that the payment of $ 252,000 of insurance proceeds from Jackson National Insurance Company ("Jackson National") to the Harrod Irrevocable Trust (the "Trust") was void; (2) whether the Bankruptcy Court erred by requiring Donald Heavrin ("Heavrin") and Bobbie Bridges ("Bridges") to reimburse the TSR bankruptcy estate for the full amount of the insurance proceeds which they received; (3) whether the Bankruptcy Court erred by requiring Heavrin to disgorge attorney's fees that TSR paid to him within one year of its bankruptcy; and (4) whether Judge David Stosberg erred by not recusing himself from these cases.

The general circumstances of these cases are well known to everyone. The Court will proceed with its analysis drawing on such parts of the evidence as is necessary.

I.

The first two issues are related and concern whether the Bankruptcy Court erred in ordering Heavrin and Bridges to reimburse the TSR estate for $ 252,000 which they received from the Harrod Trust. The Bankruptcy Court found that Heavrin's conduct amounted to actual fraud. This Court disagrees. For reasons quite different than those set out by the Bankruptcy Court, however, this Court concludes that its result is correct.

*Section 548 of the Bankruptcy Code, 11 U.S.C. § 548*, empowers a trustee in bankruptcy to avoid fraudulent transfers. The trustee may set aside transfers infected by actual fraud. Certain other transactions categorized as constructively fraudulent transfers are also subject to those same powers. The constructive fraud provision permits avoidance where the trustee can establish (1) that the debtor had an interest in property; (2) that a transfer of that interest occurred within one year of the filing of the bankruptcy petition; (3) that the debtor was insolvent at the time of the transfer or became insolvent as a result thereof; and (4) that the debtor received "less than a reasonable equivalent value in exchange for such transfer." *11 U.S.C. § 548(a)(2)(A); BFP v. Resolution Trust Corporation, 511 U.S. 531, 535, 128 L. Ed. 2d 556, 114 S. Ct. 1757 (1994).* In our circumstances, the Trustee meets all of these requirements.

A.

One could make reasonable arguments about whether a fully assigned insurance policy remains property of a bankrupt estate. This is the critical issue concerning the avoidance of the transaction.

Prior to June 17, 1994, TSR had an interest in the Jackson National policy (the "Policy"), even though it had executed a collateral assignment of the Policy to McDonald Douglas Finance Corporation ("MDFC"). Foremost, it was the legal owner of the Policy. TSR retained the right to any proceeds remaining after satisfaction of the MDFC debt. Its ownership had little actual value other than that the Policy would ultimately reduce TSR's debt to MDFC. Its interest as owner may have been a legal formality, but an interest nonetheless. Its interest in the Policy proceeds to offset the debt of MDFC was quite real and apparent. Its reverter interest, in the circumstance that the Policy proceeds exceeded TSR's indebtedness to MDFC, appeared to have almost no actual value as to the circumstances in June, 1994. Though its value may have been questionable, the interest as a matter of law cannot be ignored. Under *11 U.S.C. § 541(a)(5)(C)*, the Court finds that the Harrod Policy did constitute an interest in property of TSR as of June 17, 1994. TSR did retain an interest in the Harrod Policy.

TSR did transfer the Policy to the Harrod Trust within a year TSR filed its bankruptcy petition. The term "insolvent" is defined at *11 U.S.C. § 101(26)* to mean, generally stated, that the sum of one's debts is greater than the value of his property in a fair evaluation. Even though actual bankruptcy filing was still several months away, no one would seem to dispute that even in June TSR's debts greatly exceeded its

assets. TSR appears to have been insolvent at the time of the transfer. Thus, the second element is established.

The last remaining question is whether the debtor received a reasonable equivalent value in exchange for the transfer. This question is made somewhat easier due to the fact that TSR received no consideration for the transfer of the Policy. Previously this Court has said that the reverter interest had almost no value. In June, 1994, this certainly seemed the case. The Court should look at all the circumstances when determining whether TSR received reasonable value in exchange for such a transfer. Two events unrelated to TSR's transfer convince the Court that the absence of any consideration cannot be deemed reasonable or equitable under the whole circumstances.

As a result of the transfer, TSR lost something--MDFC eventually claimed only $ 1,750,000 rather than $ 2,000,000 as a setoff on its secured debt; and Heavrin gained something--the apparent opportunity and leverage to negotiate a $ 252,000 settlement with MDFC. Under those circumstances, the transfer created value for Heavrin and caused a determent to TSR. In return, for providing this value and undertaking a determent, TSR received no consideration. The Court concludes that the Trustee has satisfied all the requirements of constructive fraud under *Section 548(a)(2)(A)*.

B.

The Bankruptcy Code empowers the Court to employ equitable remedies to recover the value of property avoided under *Section 548* from any person who is the immediate or mediate transferee of the original transferee. *11 U.S.C. § 550(a)*. Heavrin and

Bridges fit precisely that definition as each was the immediate transferee from the Harrod Trust.

The evidence is completely confusing as to why MDFC would settle with Heavrin and agree to Jackson National paying $ 252,000 from the proceeds of the policy directly to the Harrod Trust. What cannot be seriously disputed is that the Harrod Trust did obtain those proceeds directly from Jackson National which otherwise would have reduced MDFC's unsecured claim against the TSR estate. Neither the Harrod Trust nor Heavrin can be faulted for MDFC limiting its setoff to $ 1,750,000 rather than $ 2,000,000. As a matter of equity, however, it cannot be disputed that the Harrod Trust benefitted and the creditors of TSR were harmed by this result. Consequently, both as a matter of law and equity, the Court concludes that it is proper to require repayment of the Policy proceeds from Heavrin and Bridges to the TSR estate. n1

II.

The Court must next determine whether the Bankruptcy Court erred in determining that Heavrin must disgorge approximately $ 46,000 in attorney's fees which he received from TSR within one year of the bankruptcy petition. This issue has been the subject of some difference of opinion between the bankruptcy and district courts. The Bankruptcy Court believes that because TSR reported the fees as insider payments and because Heavrin did not independently report the fees, these payments within the year prior to the bankruptcy should be disgorged. After reviewing this matter in its entirety, the Court concludes that it is best to start its analysis from scratch. This is necessary because numerous mistakes and misconceptions seem to have

invested the arguments on this issue. The Court does not excuse itself from this indictment. The basic and original assertion here is that Heavrin must be required to disgorge all his fees because he did not disclose those fees as required by *11 U.S.C. § 329*. The Court now believes that the entire premise of this assertion is incorrect.

*Section 329* requires "any attorney representing a debtor in a case under this title, or in connection with such a case" must file a statement of compensation received from the debtor within the year preceding filing of the petition. Heavrin was counsel for TSR prior to bankruptcy. He was not counsel for the debtor TSR. As yet the Court has not seen evidence that Heavrin represented the debtor while in bankruptcy. By its terms *§ 329* applies only to attorneys for the debtor and does not apply to counsel generally who provided services for a corporation prior to bankruptcy. The Court cannot find a single case in which a court applied the *§ 329* obligations to pre-petition counsel. Now reading the provision, the words seem so clear that the Court is uncertain how one could state a view so confidently to the contrary.

It does not seem to this Court that Heavrin should be sanctioned for Mr. Chinn's failure to disclose fees which TSR paid to Heavrin. The duty to disclose such fees and other disbursements bound Chinn, TSR and perhaps corporate officers, not Heavrin. Moreover, the payments were not concealed. Chinn disclosed the fees in the petition as payment to a related person.

The Court has previously conducted a perhaps overly thorough analysis of *Mapother & Mapother, P.S.C. v. Cooper (In Re Downs), 103 F.3d 472 (6th Cir.*

*1996)*. In that case, Mr. Friedman replaced the original counsel for the debtor, Downs. Friedman represented Downs in the on-going bankruptcy proceedings. Thus, *§ 329* clearly applied to him. This Court's analysis of *Downs* appears correct except for the assumption that the *§ 329* disclosure requirements bound Heavrin. Not being an attorney for the debtor, Heavrin is in a different position than Friedman. To that extent this Court has been in error.

A few other comments are in order. This Court did not intend to determine that Heavrin's services for the year preceding the bankruptcy were "in connection with the bankruptcy." Heavrin performed substantial services for TSR prior to its petition. That Heavrin was probably aware that TSR was in danger of a bankruptcy is quite irrelevant to the Court's analysis.

The thrust of the Trustee's argument seems to be that Heavrin was paid more than he deserved to receive. No one seems to disagree that Heavrin engaged in an arrangement for a $ 10,000 monthly retainer from TSR and that he performed a substantial amount of work. If this amounted to a preferential payment or a fraudulent transfer, the Trustee could have advanced such a claim. He did not make either such claim. Instead, the Trustee sought disgorgement based on Heavrin's failure to comply with his duty to report fees under *§ 329*. Absent a duty that the statute would impose if Heavrin was an attorney for the debtor, the Trustee cannot maintain a claim of disgorgement under *§ 329*.

III.

Finally, the Court must determine whether the Bankruptcy Court erred in denying Heavrin's motion

that Judge Stosberg be recused from this case. Heavrin argues that Judge Stosberg should have recused himself, mostly on the grounds of comments and rulings which the judge made during the course of the litigation. The Court disagrees.

This litigation has been hotly contested. In the course of it, Judge Stosberg has made numerous decisions which required that he assess Mr. Heavrin's truthfulness and motivation. That he made those decisions adversely to Heavrin, does not require Judge Stosberg to recuse himself. The Court agrees with Judge Stosberg's handling of the recusal motion and concludes that his denial of that motion is supported by the law and sufficient facts of record. The Court finds no basis for concluding that Judge Stosberg erred or abused his discretion in denying the motion.

The Court will enter an order consistent with this Memorandum Opinion.

JOHN G. HEYBURN II

CHIEF JUDGE, U.S. DISTRICT COURT

**ORDER**

The Court has considered numerous issues on appeal in these three cases. The Court has issued a Memorandum Opinion discussing those issues. Being otherwise sufficiently advised,

IT IS HEREBY ORDERED that the Bankruptcy Court's order determining that the payment of $ 252,000 of insurance proceeds from Jackson National Insurance Company to the Harrod Irrevocable Trust to be void is AFFIRMED.

IT IS FURTHER ORDERED that the Bankruptcy Court's order requiring Donald Heavrin and Bobbie Bridges to reimburse the TSR Trustee in the amount of $ 252,000 for the proceeds of insurance policy received is AFFIRMED.

IT IS FURTHER ORDERED that the Bankruptcy Court's order requiring Donald Heavrin to disgorge attorney's fees in the amount of $ 46,000 received from TSR is REVERSED.

IT IS FURTHER ORDERED that the Bankruptcy Court's order denying Donald Heavrin's motion that Judge Stosberg recuse himself is AFFIRMED.

This is a final and appealable order.

This 23rd day of February, 2004.

JOHN G. HEYBURN II

CHIEF JUDGE, U.S. DISTRICT COURT

Footnote

n1 The Court disagrees with the Bankruptcy Court's finding of actual fraud. *See U.S. v. Heavrin, 144 F. Supp.2d 769 (W.D.Ky. 2001)*. The evidence before the Bankruptcy Court appears similar to that which this Court considered in the criminal trial. The standard of proof, of course, is much different. Moreover, the elements necessary are different. The Court need not review the Bankruptcy Court's determination of actual fraud.

Filed 1/22/2003
Case No. 94-32848(3)7
A.P. No. 96-3129

UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF KENTUCKY

IN RE:

TRIPLES. RESTAURANTS, INC.
Debtor

J. BAXTER SCHILLING, TRUSTEE IN BANKRUPTCY FOR TRIPLE S RESTAURANTS, INC.
Plaintiff

vs.

ROBERT E. HARROD IRREVOCABLE TRUST
DONALD M. HEAVRIN BOBBIE H. BRIDGES
Defendants

MEMORANDUM

On September 23, and 25, 2002, the Court conducted a trial to determine whether the Trustee may avoid, under 11 U.S.C. § 544, § 548, § 550, and KRS 378.010 and 378.020, the transfers to Donald M. Heavrin ("Heavrin") and Bobbie H. Bridges ("Bridges") of the Debtor's interest in $250,000 of life insurance proceeds paid to the Defendants following the death of Robert E. Harrod ("Harrod"). The transfer was effectuated through The Robert E. Harrod Irrevocable Trust (the "Harrod Trust"), of which Defendants, Heavrin and

Bridges were 50% beneficiaries. Of the $250,000 paid to Defendants, Heavrin received $177,712.33 (which includes accumulated interest) and Bridges received $75,000.

At the trial, the Court heard live testimony from the following witnesses: Donald M. Heavrin, Defendant, Innes Mather, CPA, David Cantor, attorney, and Michael Forrester, insurance agent for the life insurance policy on Harrod.

The Court also considered the deposition testimony of Defendant, Bridges, and David Nelson, of McDonald Douglas Finance Corporation ("MDFC"), whose deposition was taken in this case.

Heavrin moved to admit the testimony of Michael Macatee and David Nelson from the criminal trial involving Heavrin. The Court excluded the testimony of David Nelson from the criminal trial involving Heavrin, under Federal Rules of Evidence 801(d)(1), 613, 803 and 804(b)(1). (For a more detailed recitation of the court's evidentiary ruling, see the transcript of the record at the beginning of the trial). The Court admitted the testimony of Michael Macatee from the criminal trial of Heavrin based on the consent of the parties to the introduction of this particular testimony.

Factual Background

In 1988, Harrod and Michael Macatee formed Triple S Restaurants, Inc. ("TS"), each owning one-half of the shares of the company. (Defendant's Exhibit 2). Heavrin is the stepson of now-deceased Harrod.

Heavrin also represented TS as its corporate counsel. In July of 1992, Heavrin became aware of the dire financial straights of TS. One month later, in August of 1992, Heavrin's law firm drafted an irrevocable trust, the Harrod Trust, and in September of 1992, Harrod transferred his 500 shares of stock in TS to the Harrod Trust. Neither Harrod nor TS received consideration for the transfer of TS stock into the Harrod Trust. The beneficiaries of the Harrod Trust were Defendants, Heavrin and Bridges (Harrod's daughter). The Harrod Trust designated Harrod as the Trustee, and Heavrin and Bridges were designated as successor Co-Trustees of the Harrod Trust.

MDFC financed the operations of TS. As part of the financing arrangement, MDFC required that TS acquire life insurance on Macatee and Harrod ($2M each). (Defendant's Exhs. 2 and 4). TS was designated as the owner and beneficiary of the insurance policy on Harrod's life (the "Harrod Policy"). On November 21, 1991, MDFC obtained a security interest in the Harrod Policy to secure repayment of the TS debt, pursuant to a Collateral Assignment (Defendant's Exh. 3). In August of 1993, TS stopped paying premiums on the Harrod Policy. Under the terms of a Harrod Stock Purchase Agreement, the premiums were to be paid by TS, and if a default in premiums occurred, Harrod became obligated to pay the premiums. (Defendants' Exh. 2). However, MDFC was the entity that actually made the premium payments for TS from August 1993 through September of 1994, when Harrod died. (Trustee's Exh. 23). MDFC paid the premiums on the Harrod Policy to protect its security interest under the Collateral Assignment.

On June 17, 1994, TS transferred the ownership of and

beneficial interest in the Harrod Policy from TS to the Harrod Trust. (Defendant's Exhibit 7). This is the transfer the Trustee seeks to avoid through this adversary proceeding. Also in June of 1994, with knowledge of Harrod's lung cancer diagnosis (Trustee's Exhs. 2, 3, 31, 36), Heavrin began negotiating with MDFC for himself and Bridges to receive part of the proceeds of the Harrod Policy in the event of Harrod's death, as beneficiaries of the Harrod Trust.

(Trustee's Exh. 24).

TS filed bankruptcy on September 30, 1994. On November 3, 1994, Heavrin, as Trustee of the Harrod Trust, settled with MDFC with regard to all claims the Harrod Trust had against the Harrod Policy (the parties signed mutual releases) and, under the Settlement Agreement, the Harrod Trust was to receive $250,000 of the Harrod Policy proceeds assigned to MDFC. (Trustee's Exhibit 20). After Harrod died on September 2, 1994, Heavrin received $252,712.33 (which included accumulated interest), kept $177,712.33 and sent $75,000 to Bridges, under the terms of the Settlement Agreement.

The ultimate question for this Court is whether the Defendants paid any consideration for the ultimate transfer to them of $250,000 of the Harrod Policy proceeds. Heavrin attempted to prove consideration in two ways. First, Heavrin testified at trial that the Harrod Trust agreed to make the premium payments on the Harrod Policy as consideration for the transfer. However, Defendants adduced no proof that the Harrod Trust ever made the premium payments. Rather, MDFC made the premium payments on TS'

behalf after TS defaulted. (Trustee's Exh. 4 and 23). Indeed, MDFC paid the premiums at the request of Heavrin himself. The Trustee proved this fact by introducing a letter, dated July 13, 1994, from Heavrin to David Nelson, Manager of Special Credit with MDFC, stating "Please pay!" [the Harrod Policy premiums]. (Trustee's Exh. 4)

Second, Heavrin argued at trial that the Settlement Agreement settled a lender liability claim against MDFC, however, the evidence presented at trial failed to support this assertion. Heavrin failed to establish any egregious conduct or corporate interference on which to base a lender liability claim. In fact, it was the individuals, Heavrin and Bridges, who received $250,000 of the Harrod Policy proceeds and Defendants failed to demonstrate at trial that MDFC perpetrated any lender liability conduct against them. David Nelson testified that the Settlement Agreement settled the claim of Heavrin to the proceeds of the Harrod Policy. (See Nelson's deposition at p. 15-16). Correspondence to and from Heavrin established the reason for the Settlement Agreement. (Trustee's Exh. 37). In a letter written by Heavrin on October 25, 1994, to Michael Forrester of Jackson National Insurance Company, Heavrin explained, "The Trust Fund is currently the owner and beneficiary of Jackson National Life Policy No. 0019001720 subject to the assignment in favor of McDonald Douglas Financial Services Corporation. ("MDFC")." In this letter, Heavrin explained that the Harrod Trust beneficiaries (the Defendants) and MDFC had settled for $250,000, and Heavrin enclosed a copy of MDFC's August 19, 1994 letter to Heavrin from Nelson of MDFC, which states, "I am writing to confirm our discussions concerning the referenced life insurance

policy." The letter further explains, "The disbursement of the $250,000 would represent the full settlement of all matters relating to this insurance policy."

Legal Analysis.

Trustee seeks to avoid and recover from Heavrin and Bridges $252,712.33 as a fraudulent conveyance for the benefit of the creditors in this case.

I. Trustee's Claims Under 11 U.S.C. § 544(b).

Under 11 U.S.C. § 544(b), which refers to applicable state law (K. R.S. 378.010 and 378.020),

> The trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.

KR. S. 378.010 provides,

> Every gift, conveyance, assignment or transfer of, or charge upon, any estate, real or personal, or right or thing in action, or any rent or profit thereof, made with the intent to delay, hinder or defraud creditors, purchasers or other persons, and every bond or other evidence of debt given, action commenced or judgment suffered, with like intent, shall be void as against such creditors, purchasers and other person. This section shall not affect the title of a purchaser for

> a valuable consideration, unless it appears that he had notice of the fraudulent intent of his immediate grantor or of the fraud rendering void the title of such grantor.

K.R.S. 378.020 provides,

> Every gift, conveyance, assignment, transfer or charge made by a debtor, of or upon any of his estate without valuable consideration therefor, shall be void as to all his then existing creditors, but shall not, on that account alone, be void as to creditors whose claims are thereafter contracted, nor as to purchasers from the debtor with notice of the voluntary alienation or charge.

The Trustee must prove by clear and convincing evidence that on the date of the transfer (6/17/94), TS owed at least one unsecured creditor, and that the transfers in question are voidable under K.R.S. 378.010 and 378.020. In re Akin, 64 B.R. 510 (Bankr. W.D. Ky. 1986). The Trustee demonstrated at trial that TS owed several hundred thousand in unsecured debt at the time of this transfer on June 17, 1994. (Trustee's Exhs. 33(a) - 33(c)). Also, the Trustee established TS' insolvency on that date through the testimony of TS' CPA, Innes Mather. Finally, the Trustee must prove either that the transfer was made with intent to hinder, delay or defraud TS's creditors (K.R.S. 378.010), or that no valuable consideration was provided for this transfer of an interest of the debtor, TS (K.R.S. 378.020).

The Trustee demonstrated that the transfer from TS to the Harrod Trust of the insurance proceeds to the Defendants was made with intent to defraud TS'

creditors. Where transfers involve family members, the court is required to closely scrutinize the facts, and the burden shifts to the transferees, here the Defendants, to demonstrate the absence of fraudulent intent. In re Green, 986 F.2d 145 (6t" Cir. 1993); In re Stevenson, 69 B.R. 49, 50 (Bankr. E.D. Mo. 1986). The transfer in this case involved TS, the debtor, and the Harrod Trust, of which the Defendants were each 50% beneficiaries. Heavrin was corporate counsel for TS and beneficiary under the Harrod Trust, and Harrod was the President and shareholder of TS and also Heavrin's step-father and the trustee of the Harrod Trust. Where the parties are intimately related, there is a presumption of fraudulent intent. Id. Heavrin failed to rebut this presumption of fraud through the testimony and documentary evidence introduced at the trial.

More importantly, the Trustee's evidence at trial demonstrated by clear and convincing evidence that the transfer of $252,712.33 to the Harrod Trust occurred without valuable consideration, pursuant to K.R.S. 378.020. Under the Stock Purchase Agreement dated September 2, 1988, in the event TS failed to pay the premiums, Harrod, the Insured, was designated as the party responsible for the premiums. (Defendant's Exh. 2). The Trustee demonstrated, however, that MDFC paid the premiums in order to maintain the Harrod Policy after TS defaulted in payment of the premiums. (Trustee's Exhs. 5, 22). Thus, consideration for the Harrod Policy proceeds flowed from MDFC, not from the Defendants, who actually received the money.

II. Trustee's Claims Under 77 U.S.C. § 548.

Section 548(a)(1)(A) provides,

> The trustee may avoid any transfer of an interest in property of the debtor, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily - (A) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted.

In other words, the Trustee may avoid the transfer of the ownership and beneficial interest in the Harrod Policy from TS to the Harrod Trust where the Trustee proves that the transfer is made with intent to defraud TS' creditors. The Trustee established the avoidability of the transfer under Section 548(a) for the same reasons set forth above in the Section 544(b) analysis.

Moreover, many courts consider whether there are sufficient "badges of fraud" to evidence a fraudulent transfer, including, whether the transfer was to an insider (which the Trustee established at trial, based on Heavrin's relationship with Harrod as his step-father and Heavrin's role as corporate counsel for TS); whether the parties attempted to conceal the transfer. (The Trustee demonstrated that the Defendants attempted to conceal the transfer by failing to include the transfer on question 10 to the Statement of Financial Affairs on the Debtor's bankruptcy petition); whether the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred. (The Trustee demonstrated that no consideration flowed to the debtor, but rather to the

insiders, Heavrin and Bridges); and whether the debtor was insolvent or became insolvent shortly after the transfer was made. (The Trustee proved the insolvency of the Debtor on the date of the transfer in question through Trustee Exhs. 27-29). See In re XYZ Options, Inc., 154 F.3d 1262, 1271 (11th Cir. 1998).

Therefore, the Trustee has met his burden of proof and established that the transfer is avoidable under 11 U.S.C. § 548(a). We need not discuss the avoidability of the transfer under subsection (b) of 11 U.S.C. § 548.

III. The Trustee's Cause of Action Under 11 U.S.C. § 550(a).

Section 550(a) provides the mechanism for the Trustee to recover the money transferred, here $252,712.33, from the transferees, providing,

> Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553(b), or 724(a) of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from -
>
> > (1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or
> > (2) any immediate or mediate transferee of such initial transferee.

Under the terms of the Settlement Agreement between the Defendants and MDFC, the parties agreed, and

directed Jackson National to distribute, $250,000 plus accumulated interest of the Harrod Policy proceeds to the Defendants. (Trustee's Exh. 21). Heavrin received and deposited into his account the full $252,712.33 on November 21, 1994 and subsequently distributed to Bridges $75,000 (Trustee's Exh. 25), keeping a total of $177,712.33. Thus, the Trustee may recover these sums jointly and severally from the Defendants including prejudgment interest of 8% from the date of the transfer, June 17, 1994, to the date of the Judgment, at which time interest shall accrue at the federal judgment rate of interest.

Conclusion

Clearly the transfer to Heavrin and Bridges qualifies as a fraudulent transfer, and no equitable grounds exist to permit the Defendants to retain the $252,712.33 received following Harrod's death. MDFC's business relationship involved TS, not the Defendants, and any settlement benefits rightfully belonged to TS and its creditors, not to insiders holding shares in a trust. Fiduciaries such as Heavrin owe a fiduciary duty to the corporation and its creditors. Heavrin violated his fiduciary duty by channeling this money to the benefit of insiders and to the detriment of creditors. Based on the evidence at trial, the Court must order the money received by these Defendants returned to the Trustee for distribution to the creditors of TS.
January 22, 2003

David T. Stosberg
USBJ

2/1/06

No. 04-5297

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

In Re: TRIPLE S RESTAURANTS, INC.,
Debtor,

J. BAXTER SCHILLING, Trustee,
Appellee,

v.

DONALD M. HEAVRIN,
Appellant.

JUDGES: BEFORE: BOGGS, Chief Judge, GILMAN, Circuit Judge, and CLELAND, * District Judge. * Hon. Robert H. Cleland, United States District Judge for the Eastern District of Michigan, sitting by designation.

OPINION: ORDER

The court having received a petition for rehearing en banc, and the petition having been circulated not only to the original panel members but also to all other active judges of this court, and no judge of this court having requested a vote on the suggestion for rehearing en banc, the petition for rehearing has been referred to the original panel.

The panel has further reviewed the petition for rehearing and concludes that the issues raised in the petition were fully considered upon the original

submission and decision of the case. Accordingly, the petition is denied.

ENTERED BY ORDER OF THE COURT

Collateral Assignment

Policy No. 0019001720 on the life of Robert E. Harrod issued by Jackson National Life insurance Company, Lansing, Michigan

Owner Triple S Restaurants, Inc. ("Assignor")

(1) For value received, I assign the above policy and any supplementary contracts issued in connection therewith (said policy and contracts being hereafter called the "policy") and all rights, title and interest therein (now held or hereafter acquired) together with all rights ,title and interest in and to any and all prepaid premiums now on deposit or that may hereafter be deposited with said company in connection with the policy unto:

McDonald Douglas Finance Corporation
340 Golden Shore
Long Beach, CA 90802

This assignment is limited to Face Amt.

As its interest may appear, to secure payment to said Assignee of the following liabilities.

(2)By virtue hereof, said Assignee shall, until it relinquishes its rights in writing, have sole and full power: (a) to collect from Jackson National all proceeds of the policy whether payable by death, maturity, cancellation, surrender or otherwise, including premiums refundable if the policy is cancelled or found void; (b) to surrender the policy for its cash value including the cash value of any prepaid premiums (c) to

procure policy loans for the purpose of keeping the policy in force or for part or full payment of any liability secured hereby and (d) except as provided by (3) hereof, to elect any other options or privileges under said policy, to receive all other payments accruing thereunder, and to exercise all other rights of absolute, ownership in said policy.

***

Mr. Joel Price
Jackson National Life Insurance Company
5901 Executive Drive
Lansing, Michigan 48909

Re: Collateral Assignment of Policy No. 0019001720 on the Life of Robert B. Harrod

Dear Mr. Price:

As you know, McDonnell Douglas Finance Corporation is the assignee of a Collateral Assignment with respect to the above-mentioned policy. In our telephone conversation Thursday, you confirmed that you had received the death claim as well as a letter from us informing you that the amount of the debt owed to us exceeds the face amount of the insurance policy. We believe that the insurance proceeds in the face amount of the policy should be paid to us immediately as the documentation you have provided should be sufficient for purposes of making payment to McDonnell Douglas Finance Corporation. We believe that your delay in making payment to us under this policy has damaged us, including by reason of preventing us from realizing the time value of the insurance proceeds. Therefore, we hereby demand that the full face amount of the policy (?) be paid to us immediately. If we do not receive payment by Friday, November 4, we will consider pursing our legal remedies.

Please call me if you have any questions.

Sincerely,

Scott J. Foraker

***

Any individual insured under a group insurance policy or group annuity contract shall have the right, unless expressly prohibited under the terms of the policy or contract, to assign to any other person his rights and benefits under the policy or contract, including, but not limited to, the right to designate the beneficiary or beneficiaries and the rights as to conversion provided for in KRS 304.16-180 to 304.16-200, inclusive. While the assignment is in effect, and, whether heretofore or hereafter made, the insurer shall be entitled to deal with the assignee as the owner of such rights and benefits in accordance with the terms of the assignment; but without prejudice to the insurer on account of any lawful action taken or payment trade by it prior to receipt by it at its principal office or written notice of the assignment or of the termination thereof. This section acknowledges, confirms and codifies the existing right of assignment of interests under group life insurance policies.

Effective: June 18, 1970
History: Created 1970 Ky. Acts ch. 301, subtit.14, sec, 25, effective June 18, 1970,

***

***

The Trust further understands and agrees that this full and final release is intended to cover and does cover any and all future claims not known, or which may later develop, or be discovered, including the effects or consequences thereof and including all causes of action therefor.

***

Jackson National Life Insurance Company
Jackson National Life Insurance Company of Michigan
5901 Executive Drive, PO Box 24068
Lansing, Michigan 48909
(517) 394-3400

CLAIMANT'S STATEMENT

Robert E. Harrod
Louisville, KY
406-14-2518
19001720 and 0019001720
19001720 is assigned to McDonald Douglass Fiance Co.
***

US Bankruptcy Court
Western District of Kentucky

PROOF OF CLAIM

Debtor: Triple S Restaurants, Inc.
Creditor: MDFC Equipment Leasing Corp.

Notices [to]: Mr. David Nelson
MDFC Equipment Leasing Corporation
4080 Lakewood Blvd, 6th floor
Long Beach, CA 90808-1700

***

5. Total Amount of Claim at time case filed:
$3304,165.63(Secured)
$3304,165.63(Total)

Check this box if claim includes prepetition charges In addition to the principal amount of the claim. Attach itemized statement of all additional charges

6. CREDITS AND SETOFFS. The amount of all payments on this claim has been credited and deducted for the purpose of making this proof of claim. In filing this claim, claimant has deducted all amounts that claimant owes to debtor.

7. SUPPORTING DOCUMENTS: Attach copies of supporting documents, such as promissory notes, purchase orders, invoices, itemized statements of running accounts, contracts, court judgments, or evidence of security Interests. If the documents are not available, explain. If the documents are voluminous, attach a summary.

8. TIME-STAMPED COPY: To receive an acknowledgement of the filing of your claim, enclose a stamped, self-addressed envelope and copy of this proof of claim.

Date: Nov. 14, 1994

Sign and print the name and title, if any, of the creditor or other person authorized to file this claim (attach copy of power of attorney, if any)

Name: David A. Nelson
Title: Manger, Special Credits

Penalty for presenting fraudulent claim: Fine of up to $500,000 or imprisonment for up to 5 years, or both. 18 U.S.C. §§ 152 and 3571